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## TAX EXEMPTION THROUGH TAX CAPITALIZATION A FISCAL FALLACY

Attractive catch words, even though misleading, generate powerful social forces, particularly when they are used and not explicitly repudiated by recognized authorities in the field to which they apply. In the field of taxation no idea, with the single exception of the unearned increment concept, is more powerful than the notion that owing to the capitalization of taxes, certain wealthy classes regularly escape taxation. "Tax-free bonds," "tax-exempt land values," and "burdenless taxes"<sup>1</sup> are fetching slogans. Do they stand for genuine truths? Are the theories upon which they rest and the practical conclusions drawn from these theories sound and helpful?

In the writer's belief they are not: on the contrary purchasers of securities and land, who are reputed in their purchasing to capitalize existing taxes and thereafter go tax-free, do not in a genuine or practical sense accomplish any such impossible result. When the property which they buy is taxed, such purchasers pay taxes not only in appearance but in reality. When the property which they buy is not taxed directly, such purchasers bear indirectly the average burden of taxation. In the latter case they are silent or indirect, but nevertheless genuine and real, taxpayers.

### I

While the process of capitalizing taxes and the theory of incidence based upon it are applicable to virtually every form of durable property, they are generally applied in practical discussion to taxes upon securities and land. It will be sufficient for the purposes of this paper to confine discussion to such taxes.

In the case of securities, Professor Seligman has perhaps made more constant and important use of the subtleties of this theory than any other American writer. He explains:

<sup>1</sup> T. N. Carver, *Essays in Social Justice*, p. 410.

For example, let us suppose that a corporation previously untaxed has been paying five per cent dividends on its stock quoted at par. If a special tax of ten per cent be imposed on these dividends, the stockholders will get only four and a half per cent. But since by the supposition other classes of corporations, or at all events other non-corporate investments, are not taxed, the price of the stock will fall to ninety. People who can get five per cent on their capital will not ordinarily consent to take four and a half per cent. The original holders of the stock will indeed lose, but the new purchasers will not be affected, because the tax is capitalized and leads to a depreciation of the capital value of the stock. A dividend of four and a half dollars on stock costing ninety is as good as one of five dollars on stock costing a hundred. A tax levied only on corporate profits, or only on some special classes of corporations, does not affect anyone except those who become stockholders before the imposition of the tax. To tax the new purchaser on his security would not in such a case involve unjust double taxation.<sup>2</sup>

At another place Professor Seligman restates the same point in these words:

If a corporation is taxed on its income, and if no similar tax is levied on other corporations or on other securities, the stock will fall in value and the new purchaser who buys at the reduced price really buys free of tax. Although he pays the tax, the amount of the tax is thus discounted in the depreciation of the security. With the lapse of time and the fluctuations in the market the original holders all disappear. Hence at any given time an exclusive income tax levied only on the corporation and not on the shareholder does not affect anyone except the original holders who bought before the imposition of the tax. It is only a question of time until this class of original holders disappears entirely.<sup>3</sup>

These citations are quoted primarily to illustrate the capitalization process and the concept of "exemption through capitalization." The practical application of this doubtful doctrinal tool is another matter. Professor Seligman's practical conclusions are so subtle and varied that the reader should make his own interpretation of their meaning from the original text.<sup>4</sup> The net effect of his teaching, however, and the conclusion that would be drawn by the average reader, I believe, is that where the corporation tax is "exclusive" it would be legitimate to levy another tax on new purchasers of the stock as distinguished from original owners,

<sup>2</sup> Seligman, *Essays in Taxation*, eighth edition, p. 108.

<sup>3</sup> In *op. cit.*, p. 308.

<sup>4</sup> *Op. cit.*, pp. 108-110, 308-311; and *The Shifting and Incidence of Taxation*, third edition, pp. 178, 182, 221-226, 269-270 *et passim*.

and that the principal reason for this conclusion is the contention that new or subsequent purchasers buy free from taxes.

Whether this conclusion be sound or unsound, as I view it, depends upon the character of the new tax and the circumstances which call it forth. Generally speaking the new tax will be legitimate or not according as it is general or not. If everybody has to assume a new and heavier burden it may be legitimate to place this burden upon stockholders, particularly new purchasers, who are paying through the corporation the exclusive tax. But the justification of the new tax is its generality, or the circumstances which made it necessary, not the alleged fact that the old tax was evaded or shifted through the capitalization process. The argument from "burdenless taxes" and "tax-free securities" justifies not only new general taxes but new special taxes on "subsequent purchasers."

Professor Seligman lays great stress also on the inclusiveness or exclusiveness of the old tax. But it is the exclusiveness or inclusiveness of the new tax rather than the old tax which counts. The more exclusive the old tax, the weaker is the argument for a new tax. That one class of corporations has been singled out for exclusive taxation constitutes a nominal or formal reason (see VI below) for not taxing their stockholders further, and in taxation the appearance of things is a minor but not wholly negligible consideration. But if we leave the formal aspect of things and pass to fundamentals, then a new general tax may justly be levied—if needed—whether old taxes are inclusive or exclusive or midway between. "Exemption through capitalization" has, so far as I can discover, little to do with the problem except to make mischief and supply an excuse for new taxes of a confiscatory kind. Stated in other words, the returns on various forms of investment are equalized through competition; existing tax burdens and immunities are accorded full weight in this equalization of profit or return; at any given time purchasers of taxed property stand on the same footing as purchasers of exempted property; if new taxes must be imposed, exemption in form and appearance give some ground for selecting the property which is in appearance exempt; but "exemption through capitalization" furnishes no ground for anything at all except erroneous conclusions. There is no "exemption through capitalization"—what there is, is equalization of burden through competition.

## II

A similar theory, in even more drastic and radical form, is frequently applied to land taxes. Each set of purchasers buy or secure their land after capitalizing the existing burden of taxation. They will take the land only when they can purchase it at the capitalized rental minus the capitalized burden including taxes. Unless tax rates are increased, therefore, land purchasers are thereafter tax-exempt.<sup>5</sup> If we would place landowners on the same level with other taxpayers the rate of taxation upon land must be periodically increased. If land changes hands once every thirty years on an average, then equity demands that tax rates and land shall be substantially doubled once in thirty years. By a steady increase in the rate of taxation, according as one is radically or conservatively inclined, the rate of taxation is multiplied until all economic rent—or only so much as is needed to defray public expenses—is taken.

While it may be superfluous to illustrate further the importance and application of these theories to land taxation I can not refrain from calling attention to the use made of this theory in the recent report of the (Mayor's) Committee on Taxation of the City of New York. This report will mark an epoch in the single tax movement. It is at once a tribute to Mayor Mitchel who selected the personnel of the committee, to Professor Seligman who planned its investigations and guided its deliberations, to experts like Dr. Haig and administrators like Mr. Tanzer who actually carried out the work. Almost every phase of the problem raised by the proposal to untax buildings is canvassed and covered. Now the significant thing for present purposes is that the minority, consisting of Frederick C. Howe, Lawson Purdy, Delos F. Wilcox, Frederic C. Leubuscher, and Frederic B. Shipley, in a dissenting opinion marked by singular ability, dignity, and good taste, not only use the capitalization argument but pointedly call attention to the fact that this argument is not answered by the majority. "No direct answer," say the minority on page 44 of the report, "is made to the contention that the only way to tax present land owners at all is by an increase in the tax rate on land." And they state the argument itself (p. 40) in the following words:

<sup>5</sup> Cf. C. B. Fillebrown, *State and Local Taxation* (now *Proceedings of the National Tax Association*) vol. I, pp. 286-293; also *The A B C of Taxation* and other works.

Moreover it is pointed out that every purchaser of land buys himself free from all future taxes at the established rate. The taxes are discounted in the price he has to pay for the land. He is merely the collecting agency for the city and even the cost of collection is discounted. If the tax increases by reason of an increased assessment based on an increased value, still the owner is only giving up a percentage of what comes to him *gratis*, and in reality he escapes the burden of taxation altogether unless the *rate* of taxation is increased. It is urged, therefore, that the transfer of the tax on buildings to land values would not be unjust even if it should result in some decrease in the capital value of land as reflected in the selling price, as this is the only way in which any real share at all of the burdens of government can be placed on the present owners of land, as such.

### III

The problem under consideration is not a mere question of form and appearance. So far as "subsequent purchasers" are concerned, the theory holds whether the property is paying the ordinary and usual rate of taxation or not. If the purchaser can buy himself "tax-free," it makes no difference according to this theory whether the original tax from which he frees himself is higher, lower, or exactly equal to the general or average rate of taxation on the property or income involved.

Furthermore, the problem is rather one in equity than in economics. Purchasers having bought themselves free from tax, justice requires that the tax rate shall be increased. Accepting it first of all as a problem in equity, I am forced to say that I know of no proposal in the whole field of modern taxation which is so perversely immoral as this. At the conclusion of this article I have expressed my very real admiration of the aims and service of the men who have particularly identified themselves with this doctrine. But the high character of its sponsors unfortunately does not neutralize the peculiar perversity of the doctrine itself.

The essence of the doctrine is that the purchaser is getting off tax free. In appearance he may be paying the ordinary rate of taxation or more. In fact, it is claimed, he is escaping the common burden. In other words, he unjustly enjoys some special privilege or immunity. That is the rationale of the whole doctrine and yet paradoxically the theory is built up on the assumption that the purchaser in question earns on the property after the process of capitalization only what other investors and business men are making in the same community. In other words, he enjoys no immunity; he gets no special privilege.

The doctrine is immoral, in the second place, because it leads to confiscation by taxation. Let us assume that bonds, for instance, change hands on the average about once every ten years. If this is the case and if it be the legitimate aim of the legislator to prevent any class from escaping the ordinary burden of taxation, then the inevitable conclusion (ignoring certain mathematical difficulties which do not affect the general principle) is that the government should double the existing rate of taxation on new purchases of bonds once every ten years until their entire value is absorbed. Now it should be clearly understood that Professor Seligman and some other writers who talk of "burdenless taxes," "tax-free bonds," and the like, apparently reject all such conclusions. But they do so despite and not because of "exemption through capitalization"; and it is this idea with its logical implications that I am attacking. If most men and most forms of property are paying taxes, while a fortunate group of "subsequent purchasers" is getting off "scot-free," then the average taxpayer feels ethically justified in going after the tax dodgers with an ax. The sophisticated expert may reach correct conclusions despite false premises, but the simple-minded voter wants to clap on a fair average tax every time a purchaser frees himself from the ordinary tax burden. The single taxers have had the courage of their convictions, and have pursued the "tax-free" premise to its ultimate lair, complete confiscation of land values. Those who apply this idea to the taxation of securities, however, have not usually been so inexorable in their logical processes.

But its particular perversity comes out most clearly when we consider that the increase of taxation, *i.e.*, the progressive increase in the rate, can only be carried through by deception. The purchaser must be surprised or he can not be taxed. He must be led to believe that no further increase in the rate of taxation is contemplated, because if he is not so deceived he will inevitably discount the future increases and dump the accumulated burden on others. Advise him in advance that the rate of taxation is to be periodically increased and he will appraise the property or income as a terminable annuity. To work the scheme on him you must deceive him. You must lead him to believe that the tax rate is going to be one thing and then later you must make it some other thing. Here is the essential immorality of the whole proposal. It involves deception, surprise, political ambush.

## IV

I have, of course, no belief that the men who talk of exemption through capitalization would for a moment approve any such program of deception. They would desire that the whole program, with its remorseless increase in tax rates, should be known and understood in advance. But as soon as the program is announced in advance, the whole scheme melts like the myth that it is.

Assume in the case of bonds that a fixed program of increase in the tax rate had been adopted. Assume that the debtor, the corporation that issued the bonds, the first and all subsequent purchasers, knew that the tax rate would be increased ten per cent every ten years. What would inevitably happen? Not only all the purchasers but the debtor corporation itself would have protected itself from the very beginning. Fewer men would have gone into corporate enterprises which require the flotation of bonds. In short, by an obvious process of repercussion the burden of this confiscatory tax program would through anticipation have been placed upon the customers of the industry involved. Capital would stay out of that field until prices rose so high as to justify or repay the assumption of the unusual tax burdens involved. It would be pedantic to dwell upon this obvious process. Roughly stated its results is that, so far as tax programs are adopted in the clear, honest light of open day, any unusual burden is borne by the consumer. Per contra, the consumer is the beneficiary of any openly granted tax immunity. Burdens and bounties, both, are diffused to the great body of consumers. The purchasers of durable property are neither saints nor sinners. They bear no special burdens, they reap no special benefits. They pay sometimes formally and openly, sometimes indirectly and silently, the same taxes that other people pay. Silent taxpaying is a very real and genuine phenomenon.

The process of diffusion invalidates, it would seem, practically all of the radical conclusions of those writers who would indefinitely increase the rate of taxation upon land and securities. In particular it deprives all such arguments of their basis in equity and removes the element which has given them their greatest strength, namely, the assumption or implication that certain particularly favored classes of the community are escaping taxation. All these apparent privileges are wiped out and leveled by the forces of competition. Some men buy land and rent it; some buy land and use it for manufacturing or trading purposes; some men



invest in business, some in bonds and stocks; but at any given time (assuming a certain set of preferences for different kinds of investment) the rate of return establishes and maintains itself at a given level. In any particular line of investment full cognizance is taken both of special privileges and of special burdens. No man or set of men, where competition is free, is permitted to enjoy for a long time any special immunity. No class of investors can for any length of time go "untaxed." If taxes are not paid directly they are paid silently and indirectly through the competition of capital for the extra profit represented by the absent tax.

This brings us to what I conceive to be the cardinal error of the capitalization theory of incidence as usually stated. It assumes a current rate of return or capitalization and uses it without recognition of the fact that it is vitally affected by every existing tax. Stated in terms of pure theory,<sup>6</sup> the rate of capitalization is a resultant of all known opportunities of investment and all known taxes. It registers automatically the average tax burden. When a man buys durable property he capitalizes its net yield or income at a rate which is lower when the general tax burden is high, and higher when the general tax burden is low. He pays the existing average rate of taxation through the rate of capitalization which he is forced to adopt in his calculations. The "subsequent purchaser" consequently does not buy free from tax; he buys free from any excess of taxes over the average rate. *In other words, he pays the average rate.* Professor Seligman's treatment of the capitalization process is, if I understand it, unnecessarily complicated by his introduction of the impossibly difficult concepts of exclusive and inclusive taxation. His general method is to check or qualify the effects of capitalization by reference to the exclusiveness of both the old and new taxes, both the tax on the property involved and all other taxes. If the preceding analysis be correct, this is unnecessary. The necessary element of the problem which he attempts to incorporate in this way is already represented in the rate of capitalization.

\*The statement in the text is of course too sweeping. As a practical theory of incidence it would have to be modified by recognition of those conditions which give rise to rents, monopoly profits, and other differential gains. The statement is presented as a mere corrective of current capitalization theories of incidence and like those theories assumes the modifications required by facts not here under consideration.

## V

Just as known tax burdens are dissipated, so known bounties or privileges are diffused. This applies, I think, to the "unearned increment on land," even though we recognize an unusual fixity in the supply of land. Assuming for discussion the reality of the "unearned increment," it seems plain that much if not all of it will be diffused. This diffusion takes place in the following ways, among others:

1. Much of it will be paid directly to the state in higher taxes than could be paid if the unearned increment were not expected. Much unused and presently useless land will be taxed. This is property which speculators are willing to buy and upon which they are willing to pay taxes, only because they expect to reap and benefit by the unearned increment. In addition, the anticipation of the unearned increment keeps land values constantly in advance of a fair capitalization of the present income. This is a recognized fact which the tax assessor has constantly called to his attention, and which goes far to explain the poor assessment of property under the general property tax. In progressive communities land values are nearly always higher than the present rent (implicit or explicit) capitalized at the present rate of interest on investments from which no unearned increment may be expected. For years before the higher income is realized, therefore, the state taxes it when the tax is based on capital value.

2. Similar results follow where landowners use their lands themselves. On the frontier, settlers clear the wilderness and endure great hardships wholly incommensurate with the immediate income or product, because they expect to be compensated by the unearned increment. From the first settlement and apparently continually thereafter, in the average case, the farmer works for less than day wages if we measure his reward in current income alone. He is compensated when he sells out, in the average case; and his successor starts on the same round of buying the unearned increment by accepting lower wages and paying higher taxes than would otherwise be the case, during the interval between acquisition and sale. In other words, farmers and farms are more numerous, farm products more plentiful, and farm prices lower, because of the unearned increment. The latter is diffused in part to the state in the form of higher taxes and in part to the purchasers of farm products. It is diffused to every one who eats.

3. Similarly our railroads have counted upon the unearned in-

crement to justify extensions that would not otherwise have been made; and if the land used in operation is yielding a high economic rent, that rent enters into the earnings upon which traffic rates are based. Thus in two ways the unearned increment operates to reduce railway rates; although where rates are based upon a "fair valuation" and the increment of land values is included in such valuation, the magnitude of this kind of diffusion will be reduced.

4. The manufacturer in the same way is forced to give back to the community the unearned increment which he is supposed to receive. Here the diffusion usually shows itself in the depreciation account. In many instances buildings are not depreciated at all, the owners counting upon the increment in the land value to balance the depreciation of the building. In other cases depreciation is charged at a lower rate than would be justified if no increment were expected. This is not fanciful, it corresponds to actual practice, forced upon manufacturing concerns by the pressure of competition. Here the consumer of the product gets the benefit through a reduction in the cost of production represented by uncharged depreciation.

5. Finally, tenants receive the transmuted unearned increment by a similar practice on the part of owners of residence property. They also in an effort to anticipate the unearned increment have failed to charge off depreciation on buildings. On city property in particular, owners regularly take a smaller present or current return than could be obtained on gilt-edge securities requiring little labor of management, trusting to the unearned increment to repay them when the property is sold.

Whether all the unearned increment is thus diffused, I do not know, and nobody knows. It is not impossible that, led on by the speculative lure of the unearned increment, actually more has been diffused or deferred to secure future increment than has ever been secured. Obviously it is beside the point to cite the great fortunes made through real estate ownership and speculation. The whole argument above assumes that the unearned increment is real. And the losses incurred in real estate speculation are quite commensurate with the gains. Moreover, it is to be noted that much of the apparent recent increase in real estate values is purely nominal.<sup>7</sup>

<sup>7</sup> As Professor J. L. Coulter has pointed out (*Quart. Journ. Econ.*, vol. 27, p. 13), the price of farm land in the United States increased more during the first decade of the twentieth century than it did during the entire period between the landing of Columbus and the close of the nineteenth century.

It represents in large part simple depreciation in the value of money.

Now it may be asserted that if the future increment were and always had been accurately known in advance, it would—in the case of land with an assumed fixity of supply—have been absorbed by the first occupier or settler of the land, and thereafter every purchaser would pay tribute to him. In other words, the following objection may be registered against the argument made above: “Yes, the purchaser pays or paid to the prior owner a value based on anticipated future unearned increment. But that prior owner gets the unearned increment in this case; the value of his property right was socially created. He is the real beneficiary of the unearned increment.”

Now I pause to point out that this reply stamps with peculiar and pointed injustice the proposal to clap repeated increases of taxation on “subsequent purchasers” after the manner and for the reasons proposed by Mr. Fillebrown. If there is one man who does not deserve to be singled out for attack, it is the man who has purchased land at a price or value determined by capitalizing future unearned increment.

Coming back to the first occupiers and settlers of the land, it seems plain from what can be learned of the history of land values in this country, that they reaped for the most part only a very modest speculative land value, and that they richly earned in hardship, danger, and suffering all that they got. It is unquestionably true that in the alienation of the public domain in the nineteenth century, there was widespread exploitation, waste, and graft. But those ill-gotten gains have long since been acquired and paid for by innocent purchasers. Moreover, they did not occur in connection with urban lands to which principally, the single tax doctrine is now being applied. Historically most of what is sound in the single tax theory (and in socialistic theory as well) bears upon the inheritance of property. Here is practically the only “unearned increment” or “surplus value” of any considerable extent which can withstand searching analysis.

Dismissing, however, the dim and faded figures of “original settlers” and eliminating that element of the problem represented by inheritance, what we actually have at present is this: a constant succession of innocent purchasers buying land at values based largely upon the belief that the economic rent of such land will increase, failing to secure any increment in a very large number

of cases, and actually securing it in a still larger number, but in the effort to secure it, paying more taxes than they would pay and using the land earlier and more intensively than they would use it, if the increment were not expected. I pass no verdict upon the social profitableness of land speculation, particularly in the past. I do not believe that in the past it has contributed either to a very intelligent or to a very wholesome development of our cities.<sup>8</sup> I have known land speculation to demoralize whole communities, until a majority of the population seemed devoted to no more manly or helpful activity than a misdirected effort "to catch suckers." Historically a grave indictment could easily be drawn against land speculation. But all that is beside the point under discussion: the fact (so I regard it) that competitive forces dissipate or diffuse part, all, or more than all of the so-called unearned increment.

Much light upon the nature of the so-called "unearned increment" and the reality of its diffusion, is thrown by the simple question: Would it pay the state to purchase all land held in private ownership at existing prices? If the increment is not diffused and is really unearned, then the state can get it with absolute certainty by simply buying and waiting. And the state can afford to wait longer and to discount a more distant future than can any private individual.

Few persons would advocate such an investment. Most every one would agree, I take it, that such a venture would probably prove unprofitable; and the reasons for this belief are significant. In the first place, the state would lose all taxes on unused property. At present it raises a handsome tax revenue from this source. Next, the state would sustain the enormous losses which investors in real estate suffer. Moreover, its rental returns, after subtracting the relinquished taxes on real estate, would probably be for a long time less than the interest on the capital invested. Finally, there would be suppressed all those activities, some baneful, some neutral, and many more beneficial in their effect, which are evoked at present by the effort to hasten and realize the unearned increment. If this answer to the question be correct, the real conclusion is that most of the "unearned increment" is not unearned.

\* At present the larger urban real estate companies are working with far greater intelligence and skill. They are in many instances today really making place and time utilities; in other words, they are "producing" in large degree the land values in which they traffic.

## VI

Although the unearned increment and similar privileges or immunities tend to be diffused, they are not necessarily returned to the coffers of the state. Upon this fact may be built a formal but strong argument for the increase of taxes upon any form of durable property which is in appearance exempt or which is paying less than the average rate of taxation.

It may be said, with some truth, that there is a general presumption in favor of taxation; that it is not the state's business whether the owner of untaxed property is forced to give back to consumers the benefits of this illicit privilege or not; that the state's concern is in getting directly for the public treasury a fair tax contribution; that "the public" may not be exactly identical with the body of people who benefit by the process of diffusion noted above.

There is evidently some truth in this argument. It is not only expedient that people should pay taxes; it is expedient that they should be known and seen to pay taxes.

Under the circumstances, therefore, there may be some justification for a gradual, slow, and moderate increase of taxation upon property or income which is in appearance escaping. If securities are paying no direct taxes it may be socially expedient that by equitable stages the tax rate should be increased until the tax on securities is equal to the tax on similar forms of personal property. No owner of property has acquired or can acquire a vested right in continued exemption from direct taxation.

But all this reasoning has absolutely no application to property such as real estate which is already and at the present time bearing its full quota of direct taxation. The rate of taxation upon real estate is almost universally higher than upon other forms of property. Purchasers of land can be in no practical or equitable sense tax-free. There is no justification for an increase of taxation upon real estate based upon the capitalization theory of incidence or the general class of arguments which Mr. Fillebrown and his associates have made so familiar.

## VII

The theory advanced above leads, or apparently points, to a number of rather interesting but miscellaneous conclusions which may be recorded although they can not be adequately discussed at this time.

1. The diffusion of the "unearned increment on land" rests largely upon anticipation, upon what is practically the taxation of income or rent before it exists or is actually realized. This will be regarded by most people as a strong and fortunate characteristic of our American system of levying taxes on capital values; and so far as it does assist in diffusing the unearned increment, it represents a real excellence of the American system. We do at least succeed in taxing the vacant city lot.

But it gives to our whole system of land taxation all the speculative uncertainty involved in capitalizing future uncertainties. The task imposed upon the local assessor is, when carefully analyzed, an absurdly difficult one. Some day we shall be forced to purchase certainty of assessment and appraisal by making far greater use of the more realistic income basis, although this must be done without voting to present landowners any undeserved bonus and without relinquishing the community's present share in economic rent.

2. If the diffusion of the unearned increment rests upon sound analysis, it follows by parity of reasoning that expected future increases in land taxation will in part be anticipated and diffused. Exactly what is meant by the "shifting" of a tax I do not know, nor whether that term includes those ultimate repercussive effects on prices and the welfare of the consumer which have been emphasized above. But giving a wide interpretation to the term "shifting," the analysis here presented probably justifies the conclusion that expected increments of land taxation will be shifted in large part to substantially the same classes who benefit by the diffusion of the unearned increment. There is probably ground for the belief that land taxes are in part shifted.

3. The diffusion of the unearned increment is an anticipatory process, based upon that "economic expectancy" upon which so large a part of existing land values are based. Destroy the expectancy and you prevent the diffusion. It is for this reason that single tax agitation may and does prove so costly. It tends to prevent the diffusion without in any way increasing the public revenue. For that reason the agitation ought to be suppressed in the only way in which it can be effectively or fairly suppressed, namely, by voting it down. To that end in my opinion it is expedient that constitutional clauses prohibiting specially heavy land taxes (or the classification of improvements and personal property) should be repealed. The single taxers are entitled to

an open vote upon their "reform," and so long as it is denied to them their essentially weak proposals are strengthened by essentially undemocratic restrictions. Truth does not need to cower behind the paper bulwark of a written constitution. If the advocates of fair taxation can not explode single tax claims in an open and protracted campaign upon the subject, they deserve to be beaten.

4. There is no real danger in the activities of those sincere and high-minded, but mistaken, single taxers who believe—and say so with logic and courage—that single tax means the confiscation of land values whether innocently purchased or not. That is the doctrine of Henry George and it is the doctrine of his true disciples. It is a significant fact—and a tribute to the intellectual honesty of the men concerned—that most of the single taxers on the New York (Mayor's) Committee on Taxation repudiated the proposal to tax the future unearned increment. Not the future increment but all the increment is what they are after. Confiscation and repudiation are pillars of the single tax temple; they are of the essence of the reform. "If you innocently tread on my toes," said Henry George (I quote from memory), "you may reasonably ask to be excused, but you cannot ask to be allowed to stand there forever." If legislatures, the argument goes, have voted away socially-created land values in the past, they acted *ultra vires*, and legislatures of today are justified in undoing their pernicious work. There is little question what attitude the electorate will take toward such a proposal—they will sense its injustice instantly and overwhelm it with honest ballots.

The real danger is in those halfway advocates and dissenters, on both sides of the fence, who attempt to convince themselves and others that we may rightfully increase land taxes because through the alchemies of a mysterious capitalization process, land values are untaxed at present. That theory is really dangerous because it is an attempt, doubtless unconscious, to sweeten the unsavory flavor of the genuine single tax which turns the stomach of the average voter and like too much poison is harmless because of its very excess. The great danger lies in the attempt to make sweet and reasonable what is inherently repulsive: it lies in the careless endorsement of arguments which operate to denature an essentially nauseous medicine. Even Professor Charles J. Bullock, if he is correctly quoted in the recent *Report of the [New York] Joint Legislative Committee on Taxation* (p. 169), must be



placed in the class of those who lend aid and effort to the single tax cause:

The heaviest burden will fall here [upon real estate]. But this is greatly alleviated by the fact that whenever real property changes hands, existing taxes are capitalized, so that the purchaser buys upon what is practically a tax-exempt basis.

The writer has, of course, no quarrel with the proposition that high tax rates on land are alleviated by the fact that whenever real property changes hands existing taxes are capitalized. This may be true. But that the purchaser buys upon a tax-exempt basis is, if the preceding analysis be correct, a dangerously misleading statement.

I find in reading over the preceding paragraphs that I have written more dogmatically than I feel and more emphatically than the rules of polite controversy warrant. But the emphasis may perhaps serve a useful purpose. If the position taken be unsound, it will bring down surer and swifter retribution, a speedier recognition of the true doctrine. If it is sound, it will serve to call attention to the danger inherent in the careless use of words. I have no reason to believe, it may be added, that the doctrine here defended is new. Professor Bullock in particular has frequently called attention to the diffusion of the "unearned increment" in the case of land values, and the diffusion theory as applied to taxes is of course very old. As a matter of fact, I assumed during a number of years past that the processes here described were thoroughly understood by every one who had seriously studied the incidence of taxation. More recent events, however, have convinced me either that the analysis here presented is wrong, or, if right, that it stands in need of vigorous and repeated statement.

I am anxious, however, to avoid any confusion of theories with personalities, of measures with men. For Professor Seligman, Mr. Fillebrown and others whom I have associated with the idea of "exemption through capitalization," I have only the most genuine admiration. No one can mistake their objects and aims: if they have swayed from the straight path of logic it has always been to the side of that larger public whose interests stand in such need of articulate championship. The field of taxation is in many respects a trying one. The forces arrayed there are seldom disinterested, and their thinking is frequently, perhaps ordinarily, colored by a rather short-sighted selfishness. To this battle-

ground Henry George and his followers have brought a disinterested passion which is as unusual as it is refreshing, as fine as I am forced to believe it mistaken. Nothing could be further removed from the purposes of this paper than to smirch, or attempt to smirch, the motives of those scholars and single taxers who have so earnestly attempted to think disinterestedly in a field where without them class interests would hold almost undisputed sway.

T. S. ADAMS.